

# **California Debt and Investment Advisory Commission**

## **Tools to Revitalize California Communities**

### **New Markets Tax Credit Presentation**

June 23, 2004

# Who are the players?

- Investors
- Borrowers
- Lenders (CDE)

# New Markets Tax Credit

## How it works

- Equity investment must be made to a certified CDE with tax credit allocation for a period of no less than seven years
- CDE must loan or invest money in QLICIs (Qualified Low-income community investments)
- Investor receives tax credit as long as 85 % of investment ( including principle repayment) remains in qualified investment for the seven year period
- Onerous recapture provisions for investor if CDE fails to comply

# What is the New Market Tax Credit Worth?

- Federal Credit taken over a 7 year period  
( year of investment and next 6 anniversaries)
- Credit Rate:
  - 5% in each of first 3 years
  - 6% in each of the final 4 years
- Equals 39% of amount of original investment

# **CDE Requirements (for Lender)**

- Must be a for-profit corporation.
- Must use investment to make qualified low-income community investments (QLICIs).
- Must use allocation within 5 year period.
- Must reinvest principal repayments and any pre-payments within 1 year.
- Accountable to low-income community

# Clearinghouse CDFI

- Certified as a CDE
- For-profit CDFI since 1996
- Track record of lending in low-income areas
- Total assets exceed \$70 million (including NMTC)
- Provided CRA investment credit to over 50 financial institutions
- Current on all payments to investors

# Clearinghouse CDFI

- Received an allocation of New Markets Tax Credits in amount of \$56 million
- One of 66 awardees nationwide (round 1)
- 13<sup>th</sup> largest award in the country

# Clearinghouse CDFI Business Plan

- Direct loans to for-profit and non-profit businesses, not equity investments
- Real estate secured loans no more than 80% LTV
- Debt coverage ratio 1.10 or greater
- Maintain portfolio of performing qualifying loans that can be used to replace pre-pay QLICIs

# QLICI Requirements

- Census tract is :
  - Less than 80% median family income for either state or metropolitan area (which ever is higher)  
Or
  - Poverty rate of 20%
- Three tests for businesses:
  - Gross Income 50%
  - Tangible Property 40%
  - Employee Services 40%

# **Qualified Low-income Community Development Investments (QLICs)**

## **ELIGIBLE :**

- Commercial Businesses, Offices
- Retail Stores, Manufacturing plants
- Child Care Centers , Community Centers
- Affordable for-sale Housing Developments
- Some mixed-use projects

## **NOT ELIGIBLE :**

- Residential Rental Housing, Golf Courses,
- Gaming Facilities, Race Tracks,
- Liquor Stores, Some Farming Businesses

# Funded NMTC Projects Shopping Center



# Funded NMTC Projects Offices



# Funded NMTC Projects Community Center



# Funded NMTC Projects

## Warehouse / Manufacturing



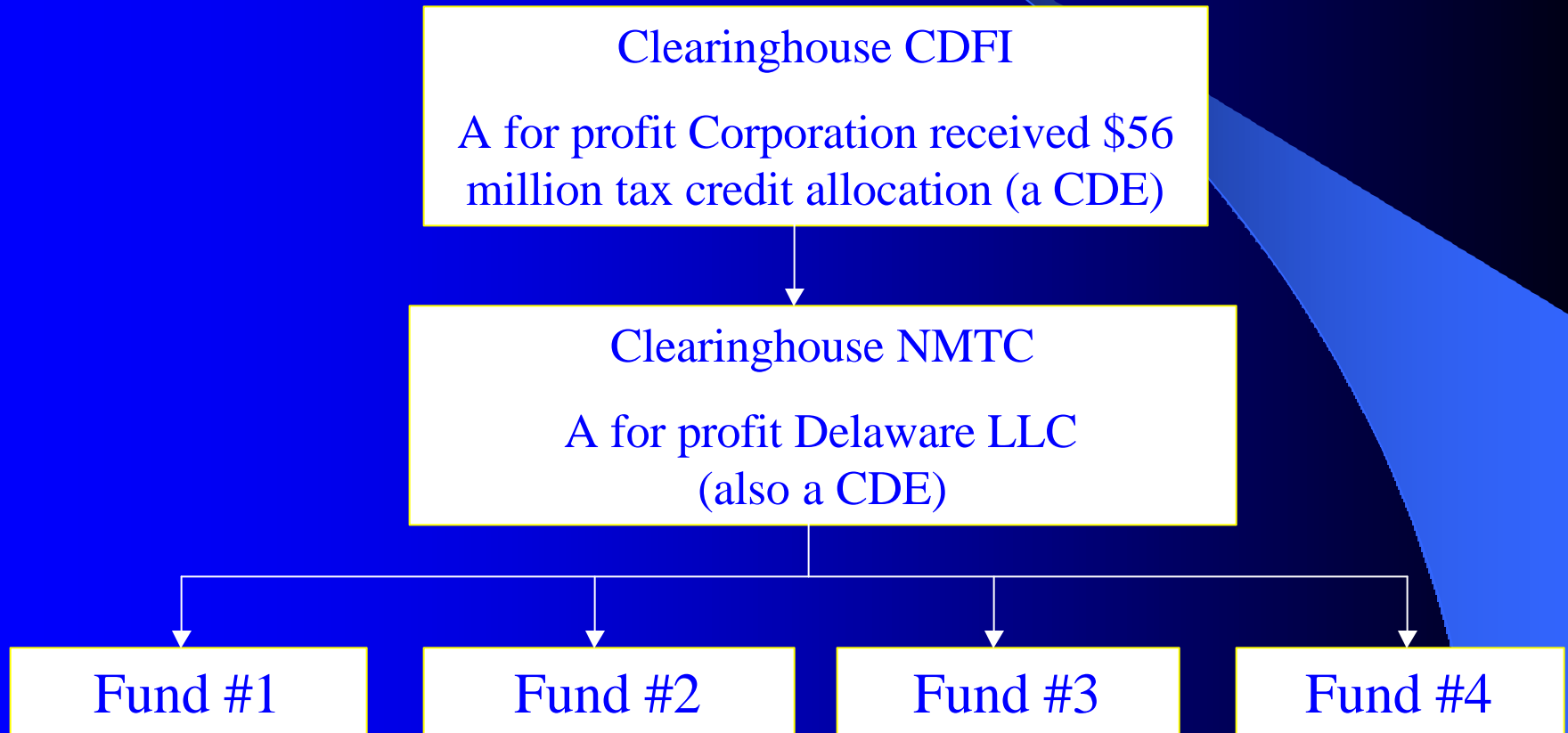
# Funded NMTC Project Churches



# Funded NMTC Project Cold Storage Facility



# Tax Credit Corporate Structure



# Investor Return

Return derived from three sources

- Tax Credit over seven year period  
( 5% in first 3 years – 6% in final 4 years) 39%
- Preferred return to shareholders  
between - 1.5% to 3% (estimated)
- Capital Proceeds (residual income)  
from LLC – Investors get 5% of total  
net profit

# IRR to investors

- Fund 1 10.09%
- Fund 2 11.29%
- Fund 3 & 4 11.95%\* (closed)

\*based on negotiated 3% return

# Compliance Monitoring

- Clearinghouse NMTC will lend 100% of investment / substantially all is 85%
- Clearinghouse CDFI will maintain portfolio of qualifying loans in portfolio for substitution if needed
- Expert staff to monitor borrower eligibility criteria

# Conventional Loan Vs. NMTC Investment

- Loan:
  - 5.75% fixed 25 due in 7
  - IRR pre tax 5.69%
  - After Tax 3.70 %
- NMTC Investment ( fund 2)
  - 2.5% preferred, Federal Tax Credit, Capital proceeds distribution
  - IRR pre tax 11.29 %
  - After tax 6.31 %

# Why make an investment?

- Competitive market rate yield
- Innovative CRA investment credit with market rate return
- Reduce/Eliminate Federal tax liability
- May also be eligible for State Tax Credit
- Immediate impact in low-income neighborhoods

# For More Information

- Contact Douglas Bystry  
President / CEO
- Clearinghouse CDFI
- (949) 859-3600
- Web site address [www.clearinghousenmtc.com](http://www.clearinghousenmtc.com)
- Thank you !